APPENDIX

In the Supreme Court of the United States

OCTOBER TERM, 1968

No. [redacted] 17

UNITED STATES OF AMERICA, PETITIONER

v.

THE DONRUSS COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

PETITION FOR CERTIORARI FILED DECEMBER 26, 1967
CERTIORARI GRANTED APRIL 22, 1968

In the Supreme Court of the United States

OCTOBER TERM, 1967

No. 963

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THE DONRUSS COMPANY

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INDEX

DOCKET ENTRIES IN THE DISTRICT COURT

April 7, 1964	Filed Complaint
June 8, 1964	Filed Answer
February 4, 1965	Filed Notice to Take Oral Deposition of John H. Daly, Treasurer of Philadelphia Chewing Gum Corp.
February 5, 1965	Filed Answers to Interrogatories and Cross-Interrogatories Propounded on Plaintiff's Behalf to J. W. Feighner
February 19, 1965	Filed Jury Verdict—Interrogatory No. 1 answered "Yes" and Interrogatory No. 2 answered "No"
March 3, 1965	Filed Judgment in favor of Donruss Co. —Plaintiff to recover $35,152.91 plus interest paid by plf. April 30, 1962—copy handed U. S. Attorney
March 11, 1965	Filed Amendment to Judgment—Plf. to recover $38,770.19 plus interest on said amount from 4/30/62 at 6%—copy mailed Tom Mitchell, Jr. and U. S. Atty.
March 11, 1965	Filed Motion for Judgment Notwithstanding the Verdict and in the Alternative for a Partial New Trial
April 2, 1965	Filed Order Overruling Defendant's Motion for Judgment NOV and for Partial New Trial
May 28, 1965	Filed Notice of Appeal by defendant
July 1, 1965	Filed Order Extending Time to Docket Appeal—copies mailed attorneys
August 4, 1965	Filed Motion for Order Directing the United States Clerk for the Western District of Tennessee to Include Certain Documents in and as Part of the Record of this Case

DOCKET ENTRIES IN THE DISTRICT COURT

August 23, 1965	Filed Order Sustaining Defendant's Motion for Order Directing the United States District Court Clerk to Include Certain Documents in the Record on Appeal
August 23, 1965	Filed copy of Order entered Dec. 16, 1964, by U. S. District Judge Allan K. Grim of the U. S. District Court for the Eastern District of Pennsylvania in matter No. "M2848"
August 23, 1965	Filed copy of Notice of Appeal to U. S. Court of Appeals for the Third Circuit from Order entered Dec. 16, 1964
August 23, 1965	Filed copy of Order entered February 9, 1965, by U. S. Court of Appeals for Third Circuit staying Order of U. S. District Court of Dec. 16, 1964, etc. Consent

DOCKET ENTRIES IN THE COURT OF APPEALS

August 26, 1965	Certified record (5 vol. pleadings and 5 vol. testimony), filed; and cause docketed.
September 2, 1965	Appearance of counsel for Appellee.
September 3, 1965	Appearance of counsel for Appellant.
September 3, 1965	Statement of Appellant as to contents of appendix
September, 17, 1965	Stipulation: Appellant's brief to 10/25/65 (Approved).
October 12, 1965	Twenty copies of Appendix to Brief for Appellant
October 25, 1965	Twenty copies of Brief for Appellant

DOCKET ENTRIES IN THE COURT OF APPEALS

October 25, 1965	Appearance of counsel for Appellant	
October 25, 1965	Proof of service of brief for Appellant	
November 20, 1965	Twenty copies of Brief for Appellee	
November 20, 1965	Proof of service of brief for Appellee	
November 29, 1965	Twenty copies of Supplement to Reply Brief for Appellee, with proof of service	
December 14, 1966	Cause argued and submitted (Before: O'Sullivan, Celebrezze and Battisti, JJ.)	
September 27, 1967	Judgment of the District Court reversed and cause remanded for a new trial	P-180
September 27, 1967	Opinion by Battisti, D.J.	10pp
October 18, 1967	Mandate issued (No costs taxed) Opinion with mandate	

COMPLAINT

[Caption omitted]

I

This is an action to recover Federal Income Tax paid by plaintiff, which action arises under and is controlled by the Internal Revenue Code of 1954 as amended, this Court has jurisdiction by virtue of Title 28 U.S. Code § 1346(a)(1).

II

Plaintiff is a corporation with its principal place of business in Memphis, Shelby County, Tennessee.

III

Plaintiff duly and regularly filed its income tax returns covering its fiscal years ended January 31, 1960 and January 31, 1961 with the District Director of Internal Revenue for the District of Tennessee and paid to said District Director the amount of income tax shown thereon to be due, within the time prescribed by law.

IV

Thereafter, the Internal Revenue Service assessed additional income tax for the fiscal year ended January 31, 1960 against plaintiff under § 531 of the Internal Revenue Code of 1954, known as the "Accumulated Earnings Tax" in the amount of $24,653.52 and also assessed interest theron [in the amount of, $3,643.36.] Thereafter, the Internal Revenue Service also assessed additional income tax for the fiscal year ended January 31, 1961 against plaintiff under § 531 of the Internal Revenue Code of 1954, known as the "Accumulated Earnings Tax" in the amount of $10,499.39 and also assessed interest thereon [in the amount of $1,085.75.] The said alleged deficiency in tax for the respective years under Section 531, together with the said interest thereon, were paid by plaintiff to the District Director of Internal Revenue at Nashville, Tennessee on or about April 30, 1962.

V

Plaintiff would show and alleges that the said deficiencies alleged by the Internal Revenue Service under § 531, et seq., of the Internal Revenue Code of 1954 were erroneously applied and that these additions to tax for each said year were illegally collected from plaintiff. The accumulated earnings as to which these additions to tax for the said years were assessed had been accumulated for the reasonable and the reasonably anticipated business needs of plaintiff. The said accumulated earnings had not been accumulated during either of the said years for the purpose of reducing, minimizing or avoiding taxation of any officer, stockholder or any other person in interest with plaintiff. Plaintiff has not been allowed the accumulated earnings credit for either of said fiscal years to which plaintiff is entitled under the Internal Revenue Code of 1954.

VI

On or about July 10, 1963, plaintiff filed with the District Director of Internal Revenue at Nashville, Tennessee a Claim for Refund covering its said fiscal year ended January 31, 1960, which claim was for the sum of $24,653.52 as accumulated earnings tax, or such larger amount legally refundable, together with legal interest. On or about July 10, 1963 plaintiff executed and filed with the District Director of Internal Revenue at Nashville, Tennessee a Claim for Refund covering its said fiscal year ended January 31, 1961, which claim was for the sum of $10,499.39 as accumulated earnings tax, or such larger amount legally refundable, together with legal interest. Both said Claims for Refund were made on Form 843, for such purposes provided by the Treasury Department and were presented and delivered to said District Director on or before July 10, 1963. On information and belief, plaintiff alleges that both said claims were processed and considered by appropriate Internal Revenue Service personnel in accordance with the Internal Revenue Code and Regulations thereunder issued by the Secretary of the Treasury.

VII

More than six months have expired since the receipt by said District Director of this plaintiff's said Claims for Refund with respect to additional tax and interest paid by it for its fiscal years ended January 31, 1960 and January 31, 1961. On or about April 8, 1964, plaintiff received by certified mail from the District Director of Internal Revenue Service at Nashville, Tennessee Form L-60 formally disallowing plaintiff's above-described Claim for Refund covering its fiscal year ended January 31, 1960 and a similar form by said District Director disallowing its above-described Claim for Refund with respect to its fiscal year ended January 31, 1961. The said Form L-60 with respect to the period ended January 31, 1960 and with respect to the period ended January 31, 1961 were both dated April 1, 1964; plaintiff's claims with respect to each of the two said years was disallowed in full by the said District Director. Plaintiff is entitled to bring this suit for refund under the provisions of Section 6532(a)(1) of the Internal Revenue Code of 1954.

VIII

The assessment of the additional tax for plaintiff's fiscal year ended January 31, 1960 and the assessment of the additional tax for plaintiff's fiscal year ended January 31, 1961 were erroneously made, said amounts of such taxes and the interest thereon were illegally collected and exacted from the plaintiff by the said District Director under color of the Internal Revenue laws.

IX

Defendant therefore owes plaintiff the aforesaid additional income tax and interest resulting from the illegal and erroneous application of the accumulated earnings tax to plaintiff's fiscal year ended January 31, 1960 and to plaintiff's fiscal year ended January 31, 1961, together with the legal interest on said amount.

WHEREFORE, plaintiff demands judgment against the defendant for the amounts set out in this complaint as owing by defendant to plaintiff and, pursuant to Title 28, U.S. Code § 2402, plaintiff demands a jury to try the issues in this action.

LUCIUS E. BURCH, JR.,
TOM MITCHELL,
Attorneys for Plaintiff
128 North Court Avenue
Memphis, Tennessee

ANSWER

Defendant, The United States of America, by and through its attorney, Thomas L. Robinson, United States Attorney for the Western District of Tennessee, for answer to the complaint herein, admits, denies, and alleges as follows:

I, II, III

Admits the allegations of paragraphs I, II and III.

IV

Admits the allegations of paragraph IV, except denies that the interest attributable to the accumulated earnings tax issue for the taxable years ending January 31, 1960 and January 31, 1961 is respectively $3,643.36 and $1,085.75.

V

Denies the allegations of paragraph V.

VI, VII

Admits the allegations of paragraphs VI and VII.

VIII, IX

Denies the allegations of paragraphs VIII and IX.

WHEREFORE, defendant prays for judgment in its favor, for dismissal of the complaint, for costs, and for such other and further relief as the Court may deem just and proper.

_____
United States Attorney

(Tr. 422) LLOYD N. BROWN, JR.

The said witness, having been first duly sworn, testified as follows:

DIRECT EXAMINATION BY MR. WHITE:

Q. State your name please, sir?
A. Lloyd N. Brown, Jr.
Q. Where do you live, Mr. Brown?
A. Washington, Arlington, Virginia.
Q. You work in Washington, D. C.?
A. Yes.
Q. Where are you from; where is your home town?
A. Manhattan, Kansas.
Q. Did you go to school in Kansas?
A. Yes.
Q. What school?
A. Graduated from high school in Manhattan and went to the Kansas State University, which is also in Manhattan.
Q. What did you do at Kansas State University? Did you have any particular area of specialty?
A. I received a Bachelor of Science Degree in Business Administration.
Q. When was that, sir?
A. In 1946.
(Tr. 423) Q. In Business Administration what was your specialty?

A. I took all the courses that they offered in accounting and I also majored in Economics.

Q. What did you do during the period of 1942 to 1945? Were you at college or in the service?

A. I was in the army.

Q. You came back after you finished the Army and went back to college?

A. Yes.

Q. Your college was split between pre-war and post-war? Is that a correct statement?

A. Yes.

Q. Now, what do you do in Washington?

A. My job currently is to receive reports of examinations and make an analysis, and list the reports to determine whether the government is correct or whether the taxpayers are correct in this.

Q. You say you get some examinations from whom? What branch of the government are you talking about?

A. Internal Revenue agents in the field.

Q. How long have you been working for the Internal Revenue?

A. Since June, 1955.

(Tr. 424) Q. Tell us what you have done since 1955 in the Revenue Service?

A. Well, for the most of this period I was an Internal Revenue agent examining returns in the field, corporate, individual returns of all businesses.

Q. When you say "in the field" where do you mean, out in Kansas?

A. In Kansas, yes, sir.

Q. Describe the job of a Revenue Agent a little bit more if you will, please, sir.

A. A Revenue Agent's job is difficult to describe and to do. You have to go out, he must examine the books and accounts of a great variety of businesses and from his knowledge of accounting and economics and business conditions he must make determinations as to the accuracy of those returns.

* * * *

(Tr. 429) A. The other column is the current ratio of current assets to current liabilities as shown on the balance sheet of the company.

In 1950 I did not compute it because there were current assets of some working capital of some Eight Hundred Fifty Thousand Dollars and only about Five or Six Dollars worth of current liabilities. I did not even compute that.

Q. I see. When you say, looking down through 1960, 8/30 to 1, what does that mean, trying to convert that into the language of the layman?

A. That means for every thousand dollars of liability there was Eight Thousand Three Hundred Dollars worth of assets.

Q. Bring it down to one dollar and I think it would be easier for me. $8.30 to every $1.00. You say of current assets?

* * * *

(Tr. 432) Q. As shown in Column 11 would you explain how that relates to the figures in Column 5?

A. Well, as you see, opposite 1954 this Column shows One Million Six Hunderd Twenty-one Thousand Dollars in retained earnings; opposite of 1955 it shows One Thousand Twenty-one Dollars. The difference is somewhat in excess of Eight Hundred Two Thousand Dollars but there was considerable profit made during the year.

Q. It looks like to me it was right at Six Hundred Thousand Dollars difference.

A. Apparently there was about Two Million Dollars profit after taxes.

Q. How many millions?

A. Two Hundred, Two Thousand.

Q. In other words from One Million Six Hundred Twenty-one Thousand Dollars you subtract Eight Hundred Two Thousand Dollars that brings you Eight Hundred Thousand Dollars then; the profits were accumulated?

(Tr. 433) A. That is correct.

Q. Now, what happened in the working capital as of the first of February, 1955; it is down very low to One Hundred Eighty-four Thousand Dollars?

A. That is correct.

Q. Why has that one dropped way down like that if you know?

A. Well, from an examination of the return and my accounting knowledge it is very easy to see when you take Eight Hundred Thirty Thousand Dollars out of a business the working capital is bound to go down because you are either taking that much cash out or you are going to have to borrow that much, both of which reduced the working capital of a business.

Q. You say borrowing is going to reduce the working capital, why is that?

A. It is a liability and the definition of working capital is the total capital less the liability and as I said from the returns it appeared that all the borrowings were of a temporary nature.

* * * *

(Tr. 441) Q. Mr. Brown, would you refer to the exhibits and advise where, if anywhere, it states the amount of the accumulated earnings of The Donruss Company as of the end of January, 1949?

A. I believe I mentioned that that was the first amount shown in Column 5.

Q. That is that One Thousand Three Hundred Ninety-six Dollar figure?

A. That is right.

Q. Now, can you state how long a period that it took for that amount to be accumulated?

A. From the information that I have, the corporation was started in 1946, I believe.

Q. So, that would be between 1946 and this date of January, 1949?

A. That is correct.

Q. Now in Column number 2, I beg your pardon, column 3, 1964, there is a figure of Three Hundred Ninety-three Thousand Dollars. Does that include Three Hundred Seventy-eight Thousand Dollars of stock in the Tom Huston Peanut Company?

A. It does.

Q. In other words that transaction is reflected in this schedule that you have?

A. Yes.

(Tr. 442) Q. And I notice that this Column 10 you have "dividends paid" with the word "none". Would you state what significance that was all the way through?

A. I was unable to determine from the return that any dividend had been paid. It would have shown up on the return if there had been.

* * * *

(Tr. 455)

CROSS EXAMINATION BY MR. BURCH:

Q. Mr. Brown, do you know anything about the bubble gum business?

A. Only what I have studied about it in the last four or five months.

Q. You never were entangled in it before, were you?

A. No, sir.

Q. You never audited the books of a bubble gum Company?

A. No, sir.

Q. You never gave any financial advice as to bubble gum expansion or maintaining its place in industry?

A. No, sir.

Q. You stated you were on, as I understood, a position of review in Washington in which you review reports (Tr. 456) and examinations?

A. That is right.

Q. Did you review the report of the agent that made the examination of the Donruss Company?

A. I did.

Q. When did you review it?

A. I believe it was started in October of 1964, September or October.

Q. You did not review it then until after the assessment had been made, after the tax had been paid and after the suit for refund had been commenced, did you?

A. That is correct.

Q. So, your own connection with The Donruss Company is to get out the file and reports, to get ready to help the government in this lawsuit, is that the facts?

A. That is the usual purpose of soliciting so-called expert testimony.

Q. I take it that your answer to my question is yes?

A. Yes.

* * * *

DEFENDANT'S EXHIBIT No. 48

THE DONRUSS COMPANY

Fiscal Year Ended January 31	1. Current Assets	2. Current Liabilities	3. Net Working Capital	4. Dollars of Current Assets to $1 of Current Liabilities
1949	$ 885,936.63	$ 83,340.90	$802,595.72	$ 10.6 to $1
1950	872,173.32	13.53	872,159.79	
1951	1,086,770.42	95,188.47	991,581.95	11.4 to 1
1952	892,037.55	8,221.75	883,815.80	108.5 to 1
1953	657,522.60	81,734.42	575,788.18	8.0 to 1
1954	870,974.79	91,513.41	779,461.38	9.5 to 1
1955	640,156.35	455,619.90	184,536.45	1.4 to 1
1956	791,611.69	334,363.44	457,248.25	2.4 to 1
1957	815,086.51	201,152.84	613,933.67	4.1 to 1
1958	850,909.32	79,256.83	771,652.49	10.7 to 1
1959	917,418.52	148,770.18	768,648.34	6.2 to 1
1960	965,310.59	116,615.05	848,695.54	8.3 to 1
1961	993,355.72	66,743.48	926,612.24	14.9 to 1
1962	1,007,023.41	36,122.44	970,900.97	27.9 to 1
1963	1,149,409.47	156,128.68	993,280.79	7.4 to 1
1964	1,014,266.33	212,027.12	802,239.21	4.8 to 1

DEFENDANT'S EXHIBIT No. 49

THE DONRUSS COMPANY

1	2	3	4	5	6	7	8	9	10	11
						Net Profits or (Loss)				
Fiscal Year Ended January 31	Working Capital	Net Fixed Assets	Other Assets	Capital Stock	Accumulated Earnings and Profits	Gross Sales Gum and Candy Business	Farm	Gum and Candy	Total	Dividend Paid	Increase (Decrease) In Accumulated Earnings & Profits
1949	$802,595.72	$653,255.36	$ 590.00	$ 60,000.00	$1,396,441.08	—	—	—	—	—	—
1950	872,159.79	567,848.97		60,000.00	1,379,508.76	$1,139,368.89	$(117,120.88)	$100,188.56	$(16,932.32)	None	$(16,932.32)
1951	991,581.95	589,071.33		60,000.00	1,520,653.28	1,115,688.59	78,842.53	159,106.20	237,948.73	None	141,144.52
1952	883,815.80	575,287.54		60,000.00	1,399,103.34	1,725,121.98	(116,816.87)	143,621.46	26,804.59	None	(121,549.94)
1953	575,788.18	981,815.91	29,167.78	60,000.00	1,526,771.87	1,754,347.23	29,211.97	175,284.78	204,496.75	None	127,668.53
1954	779,461.88	881,119.14	21,129.45	60,000.00	1,621,709.97	1,901,854.01	(76,038.06)	262,089.57	186,051.51	None	94,938.10
	Stock Redemptions		—	(30,000.00)	—	—	—	—	—	—	(802,400.00)
1955	184,536.45	834,690.86	32,061.27	30,000.00	1,021,288.58	2,342,432.74	15,909.20	390,834.77	406,743.97	None	201,978.61
1956	457,248.25	808,745.84	6,022.74	30,000.00	1,242,016.83	2,779,061.38	(2,470.68)	451,072.07	448,601.39	None	220,728.25
1957	618,933.67	806,551.50	6,242.38	30,000.00	1,396,727.55	3,209,355.71	(63,133.33)	393,774.35	330,641.02	None	154,710.72
1958	771,652.49	720,628.58		30,000.00	1,462,281.07	2,521,384.93	(68,607.04)	202,093.90	133,486.86	None	65,553.52
1959	768,648.34	807,161.65	9,000.00	30,000.00	1,554,809.99	2,828,776.65	(66,100.15)	259,369.99	193,269.84	None	92,528.92
1960	848,695.54	798,275.90	21,736.90	30,000.00	1,638,708.34	2,577,624.79	(40,396.48)	206,411.09	166,014.61	None	83,898.35
1961	926,612.24	779,516.23	3,186.90	30,000.00	1,679,315.87	2,609,976.19	603.40	59,550.91	60,154.31	None	40,607.03
1962	970,900.97	739,356.32	3,186.90	30,000.00	1,683,444.19	2,639,848.89	(146,000.55)	122,320.38	(23,680.17)	None	4,128.82
1963	993,280.79	774,127.99	3,186.90	30,000.00	1,740,595.68	2,851,009.66	17,325.67	225,082.74	242,408.41	None	57,151.49
1964	802,289.21	841,089.31	393,186.90	30,000.00	2,006,515.42	3,338,624.65	168,914.77	329,105.23	498,020.00	None	265,919.74

CHARGE OF THE DISTRICT COURT

(Tr. 504) THE COURT: Ladies and Gentlemen of the Jury, this, as you understand, is the lawsuit against the United States of America under Federal Taxing Statutes wherein the plaintiff, The Donruss Corporation, seeks to recover a refund of Federal Income Taxes, with interest, in the total of sum of $39,882.02; That is, the total sum of $39,882.02 for the fiscal year 1960, with proper interest as of April the 30th, 1962, I believe is the date, and $10,499.39 with interest as of April the 30th, 1962 for the fiscal year 1961.

The plaintiff, The Donruss Company, here contends that the earnings of which the within accumulated earnings tax with respect to the fiscal years ending January 31st, 1960 and January 31st, 1961 was assessed, were accumulated for the sole purpose of meeting its reasonable current needs or reasonably anticipated business needs for the two years in question, and, therefore, under the Taxing Statutes herein, is entitled to a refund of the full amounts for each year here in controversy with interest paid to the Government.

For answer to the complaint filed herein, the defendant, The United States of America, denies the corporate earn-
(Tr. 505) ings for the two years in question were accumulated for the reasonable current business needs or the reasonably anticipated business needs of the plaintiff corporation. The defendant specifically contends that the earnings in question were not so accumulated but were accumulated with the intent and for the purpose of reducing or minimizing income taxes for its sole stockholder, Don B. Wiener, and that the taxpayer corporation herein is not, under the Statutes, entitled to the refund it seeks in these proceedings.

With respect to the law, it is the duty of the Court to advise you, Members of the Jury, what the governing law is and it is your duty and yours alone to determine the true facts of the case. After you determine what the true facts are, you apply those facts to the law as given you in these instructions by the Court in making up your verdict or verdicts.

It is proper for the Court in the outset, for your better understanding, to give you briefly something of the background of this lawsuit. When The Donruss Company herein paid corporate income taxes for the fiscal years 1960 and 1961 it retained certain monies as earned sur-
(Tr. 506) plus or profits for those years instead of paying it to its sole stockholder as a dividend. Thereafter, the Commissioner of Internal Revenue, upon examination of the corporation's tax returns, assessed against the corporation a total surtax of $39,882.02 on its accumulated earned surplus for the fiscal years 1960 and 1961 here in question, contending that this surplus was accumulated beyond the reasonable current business needs or the anticipated reasonable business needs of the corporation for the two separate years involved. The plaintiff corporation paid the surtax under protest and now seeks in this proceeding, as I say, to recover of the Government for the separate years herein a refund of such payment with interest.

Accumulation of earnings by corporations, you understand, is a major avenue of individual income tax avoidance. Individual proprietorships and partnerships are subject to the full impact of progressive income tax returns, whether or not the earnings are retained in the business. Earnings retained by corporations are not affected by graduated income tax returns until these earnings are distributed to the corporation's stock shareholders and only when these earnings are distributed. Congress imposed an additional tax on corporation earnings which have been accumulated in order to avoid dis-
(Tr. 507) tribution of such earnings in the form of dividends, and thus to avoid personal income tax of a shareholder recipient. Sections 531 and 532(a) of the Internal Revenue Code of 1954 impose an additional tax upon a corporation which permits its earnings and profits to accumulate instead of being divided or distributed, thus avoiding the income tax upon its shareholders. Section 533 provides that where the earnings and the profits of the corporation accumulate beyond the reasonable needs of the business, it is determinative of the purpose to avoid income tax with respect to its shareholders.

Now, here are the Federal Statutes involved. It may be helpful to read them to you at this time. They are as follows:

"Section 531:

"In addition to other taxes imposed by this chapter, there is hereby imposed for each taxable year on the accumulated taxable income of every corporation described in Section 532, an accumulated earnings tax equal to the sum of twenty-seven and one-half (Tr. 508) percent of the accumulated taxable income not in excess of $100,000 plus thirty-eight and one-half percent of the accumulated taxable income in excess of $100,000."

"Section 532(a):

"The accumulated earnings tax imposed by Section 531 shall apply to every corporation, other than those described in Subsection (b), formed or veiled of for the purpose of avoiding the income tax with respect to its shareholders or the shareholders of any other corporation, by permitting earnings and profits to accumulate instead of being divided and distributed."

"Section 533, Subsection (a):

"For purposes of Section 532, the fact that the earnings as a profit of a corporation are permitted to accumulate beyond the reasonable needs of the business shall be determinative of the purpose to avoid the income tax with respect to shareholders, unless the corporation by the preponderance of the (Tr. 509) evidence shall prove to the contrary."

Ladies and Gentlemen of the Jury, having learned what the issues are and what the applicable Statutes provide with respect to this lawsuit, you will next be concerned with the question of where the law places the burden of proof in a case of this kind.

It is the law, and the Court so instructs you, that an assessment of taxes by the Commissioner of Internal Revenue has the support of a presumption of correctness,

and the taxpayer has the burden of proving to the contrary. Therefore, in this case, the burden of proof and the Statute clearly provides is upon the plaintiff, The Donruss Company, to show by a preponderance or greater weight of the evidence that it accumulated the surplus for each of the years here in question, instead of paying them out in dividends, for the reasonable current needs, or the reasonably anticipated needs of the business, for the separate years under consideration, and not for the purpose of reducing or minimizing income taxes of its single stockholder, Mr. Wiener.

The Court instructs you, Members of the Jury, that the preponderance of the evidence in a given case is not alone determined by the number of witnesses testifying (Tr. 510) to a fact, or to a particular state of facts, but, rather, to the weight, credit and value of the aggregate evidence on either side, and of this you jurors must be the exclusive judges.

Now, where the evidence is evenly balanced or in equipoise, as we sometimes say, if you should come to such a point in your deliberations and you are unable to determine in your own minds which way the scales should turn, then the Court instructs you that you must find against that party upon whom the burden of proof has been cast and in accordance with these instructions.

Ladies and Gentlemen of the Jury, as you understand, the important and controlling issue in this lawsuit, where the plaintiff taxpayer seeks to recover a tax refund, is whether the income accumulated by the plaintiff corporation for the separate years herein was for the reasonable current business needs, or reasonably anticipated business needs of the corporation, for the two separate years, as I say, or was held back to avoid taxes on dividends of the company's sole stockholder. Stated another way, it would be for you to determine from the evidence and in accordance with the Court's instructions, whether the (Tr. 511) monies retained by the corporation were for reasonable purposes of the business or whether they were withheld to avoid personal taxes on dividends in the hands of the company's sole stockholder, Mr. Wiener.

You understand, the accumulated earnings tax, as exacted by the Government, is under a Statute, as the Court has stated, designed to defeat any plans to avoid a shareholder's just taxes. Again, as stated, after payment of regular corporate taxes by corporations, the accumulated earnings tax is an extra tax which is computed on any corporate profits or earnings which have been permitted to accumulate and which should have been distributed as dividends to the corporate stockholders.

If you find any of the earnings and profits of the plaintiff for a given year in question were allowed to accumulate beyond the reasonable needs of the business, for that particular year, this shall be determinative of the purpose to avoid the income tax with respect to its sole shareholder, for that year, unless, of course, as the Court has said, that the taxpayer proves the contrary by a preponderance of the evidence.

There is no fixed formula in Section 531 penalty case (Tr. 512) as this, Ladies and Gentlemen, for determining whether the earnings retained by a corporation are held by it for the purpose of avoiding of taxes of the stockholders or held for the reasonably anticipated needs of the business. Each case must turn upon its own peculiar facts and circumstances. There are, however, certain recognized guides which you may consider as being helpful in arriving at a correct solution of these issues. Among such tests or guides, are the following which you may apply for each of the separate years herein in your consideration of this case:

1. An accumulation of earnings is in excess of the reasonably present or current needs of the reasonably anticipated future needs of the business if it exceeds the amount that a prudent businessman would consider appropriate for the present business purposes and for the reasonably anticipated future purposes or needs of a business.

2. The business of a corporation is not merely that which it has previously carried on but includes, in general, any line of business which it may undertake.

(Tr. 513) 8. In order for a corporation to justify an accumulation of earnings or profits for reasonably anticipated needs, there must be an indication that the needs of the business require such accumulation, and the corporation must have specific, definite, and feasible plans for the use of such accumulation. Such earnings need only to be used within a reasonable time after accumulation, depending upon all the facts and circumstances relating to the future needs of the corporation. Care must be given to correctly apportion the weight of the evidence where the plans for future needs of the business are uncertain or vague.

Examples of legitimate and recognized reasons for accumulations of earnings or profits, among others, would be:

(a) Provisions for bona fide expansion of the business.

(b) Acquiring a business enterprise to the purpose of stock or assets: and

(c) Provisions for cash, inventory, and other necessary working capital for the business.

(Tr. 514) In making your determination as to whether or not the executives of The Donruss Company retained earnings during either of the fiscal years ending January the 31st, 1960 or January 31st, 1961, for the purpose of avoiding taxes of its sole shareholder, Mr. Wiener, you must look at the matter from the viewpoint of the executives of the corporation and place yourselves in the position they occupied at the time and take into consideration all the facts and circumstances then existing and seek to determine what these executives intended at that time. Some of the factors which you may take into account when making this determination for the separate years here in question are the following:

1. Funds once distributed to the corporation shareholder and subjected to income tax in his hands at a higher tax bracket would no longer have been available for reinvestment in or use by this corporation.

2. A corporation may properly expand or modernize its plant and may legally do so by using its own assets for such growth or improvements rather than
(Tr. 515) resorting to outside sources for additional funds.

3. In adopting the viewpoint and seeking to ascertain the intention or motivation of the executives of The Donruss Company with respect to that corporation's earnings for the years ending January 31st, 1960 and January 31st, 1961, you may ascertain whether those executives took into account potential tax liabilities or other contingent liabilities of the corporation in connection with their decision to retain the corporation's earnings for said period.

4. Comparative forces or factors in the gum and candy manufacturing industry, and particularly the size and financial condition of the competitors of The Donruss Company in that industry may be accepted by you as a proper reason for retaining quick assets in the business, if you find that during or at the end of the separate years in litigation here such competitive factors and the size and the condition of its competitors were considered by the executives of The
(Tr. 516) Donruss Company when they decided to retain quick assets of the business during such years.

There are several ways, the Court instructs you by which a corporation may acquire the means of financing for its proper growth and expansion. It may issue additional capital stock. It may resort to bank loans. It may plow its earnings back into the business for immediate uses. It may, absent of any ulterior motives, accumulate its earnings until the expansion can be timely undertaken. All these methods are equally legitimate. There is nothing in the law which requires a corporate taxpayer to finance its expansion by borrowings from banks or by the sale of stock to outsiders. There is nothing in the law which prohibits a corporation from plowing its earnings back into the business for immediate uses or for accumulating its earnings until, as I say, expansion is timely, that is, unless such accumulation is for some ulterior purpose.

The Court instructs you that the reasonable needs of the business for which a corporation may properly accumulate its earnings includes investing money in a customer's business in order to maintain the business of the corporation. If you find in this case that the Directors (Tr. 517) of The Donruss Company during 1960 and 1961 honestly believed that acquiring stock of Tom Huston Peanut Company would enable The Donruss Company to maintain its large volume of sales to Tom Huston Peanut Company, and planned to buy such stock, when available, then you may consider whatever amount of its funds you find were retained during those years for the purpose of buying Tom Huston Peanut Company stock was retained for a reasonable business need.

Ladies and Gentlemen of the Jury, the Court instructs you that the directors or offficers of a corporation must, in Federal tax matters, be given some discretion and some latitude in deciding what constitutes the reasonable needs of the corporate business managed by them; the test of what the reasonable needs of a corporation may be, set up by Section 531 of the Internal Revenue Code, pertains only to the honest belief of a corporation's executives that the existing accumulation was no greater than was reasonably necessary: Another way of expressing this test is by saying that the accumulation of earnings or profits by a corporation is excessive when it exceeds the amount that a prudent businessman would consider appropriate for the present or the reasonably anticipated future needs of the business.

Members of the Jury, the mere possibility that earn- (Tr. 518) ings and profits will be used for a business purpose at some indefinite time in the future is not sufficient to make the accumulation reasonable.

To make the accumulation reasonable, the plans for expansion or conversion must have substance as an existing reality in the separate years here involved. The mere recognition of a future need is not sufficient under the law to justify an accumulation.

So, if you find from the evidence that The Donruss Company merely contemplated the possibility of future expansion, without any plan of substance in existence

during either of the fiscal years 1960 and 1961, the accumulation of earnings would appear unreasonable and the company must overcome the presumption that the accumulation was for the purpose of avoiding the shareholder's income taxes. In order to determine whether profits were accumulated for the reasonable needs of the business, or to avoid taxes of the shareholder, the controlling intention is that manifested at the time of accumulations not subsequently declared intentions which may be merely the products of afterthoughts. The intention must have been manifested by some course of conduct at the time of the accumulations.

(Tr. 519) In considering whether the accumulations for the corporation herein were unreasonable during the fiscal years in question, you should, as the Court has tried to make clear, consider whether the amounts of earnings and profits on hand at the beginning of each year in question were adequate for the reasonably anticipated needs of the business as seen at the end of each of the taxable years.

Consideration, Members of the Jury, you understand, should be given to reasonably anticipated needs as they existed at the close of a tax year. Subsequent events should not be used for the purpose of showing that the retention of earnings and profits was reasonable at the close of a tax year, if none of the elements of reasonably anticipated needs were present at the close of such tax year. Subsequent events, however, may be considered to determine whether the plaintiff in this case, The Donruss Company, actually intended to consummate any plans for which the earnings or profits were allegedly accumulated.

A corporate taxpayer may, if the Court has not already said so lawfully accumulate sufficient earnings and profits to provide against reasonably foreseeable business risks, and if you find from the preponderance of the evidence (Tr. 520) in this case, that any or all of the accumulations were for such purposes, such accumulations would not be subject to the imposition of any surtax or penalty.

A corporation, again as the Court has probably already stated, is not required by law to distribute all of its earnings even thought it may be able to borrow operating

capital for its present or foreseeable needs. If you find from a preponderance of the evidence that the earnings and profits in this case were accumulated with a reasonable anticipation of avoiding the necessity of borrowing in the future, such accumulations would not be subject to the imposition of any surtax or penalty.

Ladies and Gentlemen of the Jury, the Court instructs you that the directors and officers of the corporation are permitted in Federal tax matters, as here, some discretion and some latitude as to what constitutes the reasonably anticipated needs of the corporate business.

In resolving the question of whether the accumulated earnings in this case were retained for the reasonable business needs or the reasonably anticipated needs of the (Tr. 521) corporation for the fiscal years herein, the Jury may look to direct testimony which might throw light on the needs involved and to all other proved facts from which inferences may be drawn, tending towards support or rejection of contentions of the parties with respect to the ultimate facts in this case.

The Court instructs you that nothing in the law prohibits a corporate taxpayer from purchasing 50 percent of its stock held by one stockholder, if the acquisition of such stock is for the purpose of promoting harmony or efficiency of management of the corporation or to enable the corporation to continue its accustomed practices or policies. The acquisition of 50 percent of its outstanding stock from one stockholder by a corporation does not serve as any basis for the imposition of the penalty imposed by Section 531 and related sections of the Internal Revenue Code, unless you find that such acquisition was a planned tax avoidance device and that the earnings and profits of the business had been accumulated during some period prior to the acquisition by the corporation of one-half of its outstanding stock to give effect to the planned tax avoidance schemes.

(Tr. 522) As stated, Ladies and Gentlemen, the issues in this case arise under the Statutes that Congress has enacted which provide in substance that a corporation must pay a tax called accumulated earnings tax, if it does not distribute to its stockholders all accumulated earn-

ings in excess of what is reasonably needed by the business or in excess of the reasonably anticipated needs of the business.

The factual disputes between the parties of which you are the sole judge, may be presented to you in a number of ways. However, boiling the issues between the parties down, there remains three or four basic factual disputes with respect to the two years here in question, and the Court in this trial calls upon you jurors to resolve these disputes as follows:

First: What were the reasonable needs, or the reasonably anticipated needs of The Donruss Company for working capital to meet its normal business needs as of January 31, 1960 and January 31, 1961.

Second: As of January 31, 1960 and January 31,
(Tr. 523) 1961, did the Donruss Company have any fixed, definite, certain plans for expansion or diversification or the like that would require a retention of working capital in excess of the normal needs of its business?

Three: If you answered the last question in the affirmative, for either or both of the years under consideration, only then will you answer this question: What were the reasonable needs or reasonably anticipated needs of The Donruss Company for working capital, in excess of the working capital needed to meet its normal business needs, you understand, in order to finance fixed, definite, certain plans for expansion or diversification as of January 31, 1960 and January 31, 1961?

Four: Was The Donruss Company during the years ending January 31, 1960 and January 31, 1961 availed of for the purpose of avoiding income tax liability of its sole shareholder, Mr. Donald Wiener?

(Tr. 524) Now, the Court has instructed you generally with respect to certain legal principles that you must apply in your consideration of this case and in answering each of the four questions mentioned by the Court.

Now, more specifically, in answering question number one with respect to the working capital requirements of The Donruss Company to meet its normal business needs, the Court instructs you that:

Working capital is the excess of The Donruss Company's current assets over liabilities. By this is meant that it is the excess of the aggregate of the cash, accounts receivable, inventory, and other current assets over the incurred liabilities which will have to be paid by The Donruss Company within one year.

You then determine the reasonable needs or the reasonably anticipated needs for working capital for the normal business needs of The Donruss Company. The words "reasonable needs" are used in the objective sense, that is, they mean what is reasonable to the average prudent and informed businessman. The words "reasonably anticipated needs" simply, of course, refer to the question as to what the management of The Donruss Company reasonably anticipated its needs for working capital to (Tr. 525) be for the years in question. If you find from the evidence that the management of The Donruss Company never considered or anticipated how much working capital they had to have for normal business needs for the years under consideration, then you are instructed that you must answer Question No. 1 with regard only to what the average prudent and informed businessman would consider working capital for normal business needs.

Working capital needs of a business will among other things depend upon the nature of the business, its credit policies, the amount of inventory and rate of the turnover, the amount of the accounts receivable, and the collection rate thereof, the availability of credit to the business, and similar relevant factors.

An accumulation of working capital for such things as unexpected demands of the business or unanticipated emergencies are unreasonable and cannot be considered by you in determining the reasonably anticipated working needs of The Donruss Company for working capital.

An important question here is whether in the light of the business needs of the corporation, it was reasonable to keep on hand the working capital it had as of January

(Tr. 526) 31st, 1960 and January 31st, 1961. In making up your minds about this, it is, of course, proper for you to review the conduct of the corporation during prior years and consider the financial history of the corporation.

The second and third questions you will be called upon to answer, you recall, have to do with whether The Donruss Company as of January 31st, 1960 and January 31st, 1961, had any fixed, definite, certain plans with respect to the expansion or diversifications that would require it to accumulate working capital in excess of its normal business needs, and if so, how much working capital was required? The Court, in this connection, instructs you:

First, it is important that you understand that we are talking about expansion and diversification, which is beyond and above the usual routine acquisitions of equipment and buildings that The Donruss Company has made regularly throughout its life.

To be more explicit, a business, if it is to continue, must constantly replace equipment as it wears out, and purchase additional equipment where it become available. Our tax laws in this connection permit a taxpayer to recover his costs of the assets rateably over their useful lives. In other words, if a taxpayer buys a piece of ma-
(Tr. 527) chinery for $1,000 and the machinery will last three years, he is permitted under the law to depreciate one-third of value of the equipment in each of those three years. Over the three-year period, the taxpayer would receive a deduction, because of the consumption of the piece of equipment in the business operation. This concept of allowing a taxpayer a deduction over a period of time on the cost of the equipment is called depreciation. Under the concept of depreciation, which has been talked about in this case, a taxpayer is permitted to use any benefits therefrom in any manner he desires.

During The Donruss Company's years ending January 31st, 1960 and January 31st, 1961 it, as the Court understands from the proof, claimed and was allowed by way of depreciation aggregate amounts of $137,634.98 and $150,437.74, respectively, these amounts were not in-

cluded in the plaintiff corporation's accumulations of earnings and profit. These benefits, when claimed by the taxpayer, may be utilized by the taxpayer for replacement of plant equipment or may be held for expansion or diversification purposes, among other things.

As of the end of January, 1961, The Donruss Com-
(Tr. 528) pany, it is contended by the defendant, could expect to recover similar depreciation deductions for future years in amounts in excess of $120,000 per year. Such deductions, as I say, could be utilized for replacement of equipment or other purpose of the corporate taxpayer.

So, on the subject of depreciation, the Court instructs you that you are to consider depreciation simply as another factor taken into account by the directors of The Donruss Company, when they decided to retain earnings as of January 31, 1960 and January 31, 1961. In that consideration of depreciation, you should determine from the testimony in the case what the viewpoint and belief of those directors was at such time concerning the depreciation.

The depreciation, according to the proof, claimed by The Donruss Company allowed in the years January 31, 1961, 1962, 1963 and 1964, as you will recall, was approximately $141,000 and $121,000, and $135,000 respectively.

So, it is necessary that you understand before attempting to answer Question No. 2 that each tax year in question The Donruss Company was allowed deductions as depreciation on equipment it owned and was free to take
(Tr. 529) advantage of same as it saw fit in the operation of its business. The purpose of the depreciation allowance, to further explain, is to afford the owner of a wasting asset used in any trade or business, a means of recouping, tax-free, his investment in that property.

Question No. 2 refers to fixed, certain, definite plans. For there to be a fixed, certain, definite plan, it must be established by the evidence, in case it is not clear to you, that The Donruss Company had one or more specific requirements, plans or objectives in mind which required a reasonably definite amount of money. A nebulous plan

to expand or to invest in some future and indefinite time is not a fixed, certain, definite plan.

Definiteness of the plan coupled with action taken toward completion of the plan must be present as of January 31, 1960 and January 31, 1961 before it is possible to say that The Donruss Company had such definite plans.

Although The Donruss Company could not predict with certainty that its business could continue to increase, and that its earnings would continue as they had in the past, the fear of competition and fear of lack of liquidity, (Tr. 530) that is, having a lot of working capital, must be reasonable before they justify an accumulation of earnings and working capital. Businesses generally meet competition with like types of businesses, and must maintain their assets and equipment, but fear of competition alone, particularly when the business records of earnings in the past does not justify such fear, does not warrant accumulation of working capital and earnings. Likewise, reasonable businessmen realize that they might lose some existing customers and thus, sources of revenue. But this alone does not justify the accumulation of working capital and earnings.

You will notice that in stating Question No. 2, the Court uses the dates January 31, 1960 and January 31, 1961. The Donruss Company's fixed, definite, certain plans for expansion and diversification, if any, must, as the Court again reminds you, have been formulated as of those dates. The fact that The Donruss Company expended some of its working capital after January 31, 1960 or January 31, 1961 is not determinative. The critical and crucial facts are did The Donruss Company have definite, fixed, certain plans at each of these dates (Tr. 531) to make the expenditures in the future. If you find from the evidence that they did not have such plans, then as a matter of law, you must find that it was not reasonable to accumulate working capital and earnings for expansion, diversification, or the like.

In this case, The Donruss Company has the burden of proving that it contemplated expansion or diversification in excess of the routine replacement of equipment and it must also show that such was a real consideration as of

January 31, 1960 and January 31, 1961: And, as the Court has already pointed out in these instructions, not simply as an afterthought to justify the presence of the working capital and earnings.

You, Members of the Jury, are the sole judges of the facts surrounding this controversy, and in order for you to determine what the true facts are, you will be called upon to weight the testimony of all the witnesses who have appeared before you, giving to this evidence the weight, faith, credit and value you think it is entitled to receive. You will note the manner and demeanor of the witnesses on the witness stand, whether the witness impresses you as a witness who was telling the truth, or one who is not frank in his expression in answering questions: Consider the reasonableness or unreasonableness of the (Tr. 532) testimony of the witness: The opportunity or lack of opportunity of the witness for knowing the facts about which he testifies, his intelligence or lack of intelligence: The interest of the witness in the results of the trial, if any, and the relationship of the witness to either one of the parties litigant, if any. These are the rules which should guide you, along with your common experience, common observation, and common judgment in weighing the evidence introduced for you.

If there is a conflict in the evidence, it is your duty to reconcile the same, if you can, for the law presumes that every witness has attempted to testify to and has testified to the truth. But if you should find a conflict in the evidence and are unable to reconcile the same in accordance with these instructions, then it is with you absolutely to determine which ones of the witnesses, you believe, have testified to the truth and which ones you believe have testified falsely. Immaterial discrepancies do not affect the witness' testimony or credibility but material discrepancies do.

There are several methods of impeaching or discrediting a witness. One is to prove that a witness at different (Tr. 533) times made conflicting statements as to the material facts in the case as to which he testified. Another method is by rigid cross-examination to involve the witness in contradictions and discrepancies as to the ma-

terial facts stated by him. Immaterial discrepancies in statements of witnesses do not affect their credibility unless there is something to show that they originate in wilful falsity. And you, Members of the Jury, are to determine how far the testimony of any impeached witness in this case has been impaired by either of these invalidating processes is the question to be decided by the Jury like all other questions of fact.

The issues in this case and the respective contentions of the parties are evidence enough, the Court feels sure. If you find that the plaintiff corporation did accumulate earnings beyond a reasonable present or current needs of its business, or its reasonably anticipated business needs, for the fiscal years ending January 31, 1960 and 1961, and you further find that the purpose of such accumulation was to avoid payment of taxes by the sole shareholder of the plaintiff corporation, Mr. Wiener, then your verdict for each year herein should be for the defendant, The United States of America.

(Tr. 534) On the other hand, if you find by a preponderance of the evidence that the accumulation of earnings and profits by the plaintiff corporation, as aforesaid, was for the plaintiff corporation's reasonable current or anticipated business needs, and was not for the purpose of avoiding payment of individual tax by its shareholder, Mr. Wiener, then your verdict, or verdicts, would be for the plaintiff in this case.

Now, Ladies and Gentlemen of the Jury, the Court has stated briefly the contentions of the parties with respect to this litigation. Their contentions have been set up in the pleadings, which have been explained to you, and issues made and argued to you by counsel, and it is now for you to say under these controverted issues where the weight of the evidence lies. Bear in mind, as the Court has said, that it is the duty of the plaintiff taxpayer to show by the greater weight or preponderance of the evidence of the earnings herein for the separate fiscal years were accumulated for the purpose of meeting the reasonable current business needs or reasonably anticipated business needs of the plaintiff corporation herein and not

for the purpose of avoiding additional personal tax with respect to its lone shareholder.

(Tr. 535) If, Ladies and Gentlemen of the Jury, after a careful consideration of the evidence in the case and the instruction here given you by the Court, you find that the plaintiff taxpayer has shown by the proper quantum of proof, that is, by the greater weight or preponderance of the evidence, that the earnings here in question for the two years under consideration, were accumulated for the purpose of meeting the reasonable business needs or reasonably anticipated business needs of the plaintiff, The Donruss Company, herein, rather than for the purpose of avoiding taxes with respect to its sole shareholder, Mr. Wiener, you will find for the plaintiff, for each year, and report to the Court accordingly.

If, on the other hand, you find that the earnings were not accumulated for the corporation's reasonably current or anticipated business needs, but for the purpose of avoiding personal income taxes with respect to its sole shareholder, Don Wiener, you will, in that event, find for the defendant, The United States of America and report verdicts in its favor.

At times, Ladies and Gentlemen, throughout the trial the Court has been called upon to pass on the question of whether or not certain evidence might be properly admitted. With such rulings and the reasons for them you (Tr. 536) are not concerned. Whether offered evidence is admissible is purely a question of law and from a ruling of such question you are not to draw any inference as to what weight should be given the evidence or as to the credibility of a witness.

In admitting evidence to which an objection was made the Court does not determine what weight should be given such evidence. As to any offer of evidence that was rejected by the Court, you, of course, must not consider the same: As to any question to which an objection was sustained, you must not conjecture as to what the answer might have been or as to the reasons for the objection.

In an effort to be helpful, Ladies and Gentlemen, the Court suggests the attitude or conduct of jurors at the outset of their deliberation as matters of considerable im-

portance. It is not discreet for a juror upon entering the jury room to voice emphatic expressions of his opinion of the case or to announce his determination to stand for a certain verdict. When one does that at the outset his sense of pride may cause him to hesitate to recede from an announced position if and when shown that it is fal-
(Tr. 537) lacious. Remember that you are not partisans or advocates in this matter but are in reality judges. The final test of the quality of your service will ride in the verdict or verdicts which you return to this courtroom, not in the opinions any of you may hold as you retire. Bear in mind that you will make a definite contribution to efficient judicial administration if you arrive at a just and proper verdict in this case. To that end, the Court reminds you that in your deliberations in the jury room there can be no triumph other than the ascertainment and declaration of the truth.

Preliminarily to your being accepted and sworn as jurors in this case you were examined by counsel for both the Government and the defendant as to your competency and qualifications to act as jurors in this case. As a part of such examination, each of you answered all questions asked by counsel. Your answers showed that you were competent and qualified to act as jurors in this case, and the parties accepted you as jurors on the face of your answers. The answers you then made to said questions in regard to your competency, qualifications, fairness, lack of prejudice and freedom from passion and sympathy are as binding on you now as they were then and should
(Tr. 538) so remain until you are finally discharged from further consideration of this case. It would be improper for you to disregard the answers that rendered you competent as jurors.

Ladies and Gentlemen of the Jury, appropriate forms in the nature of interrogatories will be furnished you in the jury room, upon which you may indicate your decisions concerning these matters.

Any answer that you give to the interrogatories should be signed by a foreman selected by you after you retire to the jury room and, of course, your answers must be unanimous agreement. You should not agree to any an-

swer through a gambling or speculative process. Considerations of prejudice or sympathy should not enter into your deliberations one way or another.

In considering your answers to the interrogatories, you are not to single out any certain parts or any particular point, or instructions, and ignore the others, but you are to consider all of the Court's instructions as a whole and to regard each in the light of all the others.

* * * *

REFUSAL TO CHARGE DEFENDANT'S REQUESTED INSTRUCTION NO. 15

"Defendant's Requested Instruction No. 15

Refused—Boyd, J.
2-18-65

"The Court instructs you it is not necessary that avoidance of shareholder's tax be the sole purpose for the unreasonable accumulation of earnings; it is sufficient if it is one of the purposes for the company's accumulation policy."

* * * *

INTERROGATORIES

1. Did plaintiff corporation permit its earnings or profits for the following years to accumulate beyond the reasonable or reasonably anticipated needs of its business?

Year ended January 31, 1960 Yes √ No____
Year ended January 31, 1961 Yes √ No____

2. Were such accumulations retained by plaintiff corporation for the purpose of avoiding the income tax on its stockholder, Don Wiener?

Year ended January 31, 1960 Yes____ No √
Year ended January 31, 1961 Yes____ No √

/s/

.....
Foreman

This 19th day of February, 1965.

JUDGMENT

This cause came on for trial before the Honorable Marion S. Boyd, Judge, and a jury at Court held in the City of Memphis on the 15th day of February, 1965.

And it appearing that the two principle issues in this cause, which, if either were decided favorably to plaintiff, would be the only issue in this cause, were whether or not the earnings of the Donruss Company had been permitted by that corporation to accumulate for the year ended January 31, 1960 or for the year ended January 31, 1961 beyond the reasonable or the reasonably anticipated business needs of that corporation and, secondly, whether or not the corporation, the Donruss Company, was availed of for the purpose of avoiding the income tax on its stockholder, Don Wiener, for the fiscal year ended January 31, 1960 or the fiscal year ended January 31, 1961.

And it further appearing that the said questions of fact were submitted to the jury in the form of interrogatories, agreed upon by counsel for both parties, which interrogatories and the answers made thereto by the jury were in words and figures, as follows:

"1. Did plaintiff corporation permit its earnings or profits for the following years to accumulate beyond the reasonable or reasonably anticipated needs of its business?

Year ended January 31, 1960 Yes x No____
Year ended January 31, 1961 Yes x No____

2. Were such accumulations retained by plaintiff corporation for the purpose of avoiding the income tax on its stockholder, Don Wiener?

Year ended January 31, 1960 Yes____ No x
Year ended January 31, 1961 Yes____ No x

/s/ W. Gordon Morris
Foreman

This 19th day of February, 1965."

And it further appearing that the plaintiff is entitled to judgment on said verdict of the jury.

And it further appearing that on or about April 30, 1962 plaintiff paid an alleged tax deficiency assessed against it under Section 531 et seq. of the Internal Revenue Code of 1954 with respect to its year ended January 31, 1960 in the amount of $24,653.52 and interest thereon in an amount to be determined by defendant and further that on said date plaintiff paid an alleged tax deficiency assessed against it under said Code Section in the amount of $10,499.39 and interest thereon in an amount to be determined by defendant with respect to plaintiff's taxable year ended January 31, 1961.

It is, therefore, ORDERED, ADJUDGED AND DECREED: That plaintiff, the Donruss Company, a corporation, have and recover of defendant assessed tax for 1960 and 1961 in the total amount of $35,152.91 plus interest paid thereon by plaintiff April 30, 1962, as may be determined by defendant, plus interest as allowed by law on said tax and interest from the date of payment thereof by plaintiff, April 30, 1962.

MARION S. BOYD
Judge

DATE: 3/3/65

APPROVED:

TOM MITCHELL, JR.
Attorneys for Plaintiff

A TRUE COPY.

ATTEST:

W. LLOYD JOHNSON, Clerk
By V. LAFON, D.C.

AMENDMENT TO JUDGMENT

By consent of the parties, as evidenced by the signature below of attorneys for same, the judgment heretofore entered in this cause March 3, 1965 is amended by the following addition thereto. This addition is made pur-

suant to the language in said judgment that interest paid upon taxes assessed against plaintiff for 1960 and 1961, "as may be determined by defendant" would be recoverable by plaintiff. Defendant has now determined and computed the amount of such interest. That computation as part of a schedule entitled "Summary Statement" is attached hereto and made part hereof as Exhibit 1.

Pursuant to the attached computation and by agreement between the parties hereto,

It is ORDERED, ADJUDGED AND DECREED:

1. That plaintiff shall have and recover of defendant interest assessed against and paid by plaintiff with respect to additional taxes for its fiscal year ended January 31, 1960 in the amount of $2,978.68.
2. Plaintiff shall have and recover of defendant interest assessed against and paid by plaintiff with respect to additional taxes for its fiscal year ended January 31, 1961 in the amount of $638.59.
3. Plaintiff is entitled to have and recover of defendant refund of additional taxes for its fiscal year ended January 31, 1960 and January 31, 1961, plus interest paid by plaintiff thereon, in the total amount of $38,770.18 plus interest on the said total $38,770.18 from April 30, 1962 at the rate of six (6%) per cent according to law.

MARION S. BOYD
Judge

DATE: March 11th, 1965

APPROVAL AND CONSENT

TOM MITCHELL, JR.
Attorneys for Plaintiff

UNITED STATES OF AMERICA

By: THOMAS L. ROBINSON

A TRUE COPY.
ATTEST:

W. LLOYD JOHNSON, Clerk
By W. LLOYD JOHNSON

MOTION FOR JUDGMENT NOTWITHSTANDING THE VERDICT AND IN THE ALTERNATIVE FOR A PARTIAL NEW TRIAL

Defendant, by and through Thomas L. Robinson, United States Attorney for the Western District of Tennessee, moves the Court to enter an order setting aside the jury's answer to the special interrogatories rendered herein on February 19, 1965, and entering a judgment for defendant in accordance with defendant's motion for a directed verdict at the conclusion of plaintiff's case, and the renewal thereof at the conclusion of all of the evidence, particularly upon the following ground:

1. Since Don Wiener knew he would have to pay income tax on any dividends paid to him by plaintiff during the plaintiff's fiscal years ending January 31, 1960, and January 31, 1961, and since Don Wiener was actively engaged in directing the business affairs of plaintiff, such knowledge must be imputed to the plaintiff corporation. Once this is established, as it is in this case, viewing all of plaintiff's evidence in a light most favorable to it, and resolving all of the conflicts in the evidence in plaintiff's favor, reasonable men could not differ in reaching the conclusion that the failure of Donruss Company to pay dividends was for the purpose of avoiding the income tax of Don Wiener regardless of what other purposes for accumulating plaintiff's earnings it may have established. In other words, even without weighing the credibility of the witnesses, there can be but one reasonable conclusion as to the verdict of whether the purpose of plaintiff's accumulation of earnings was to avoid the income tax of Don Wiener, regardless of what other purposes for the accumulation plaintiff may have established.

* * * *

3. Defendant was substantially prejudiced at the trial of this case because of each and the aggregate of all the errors made by the Court, as follows:

* * * *

(g) The Court submitted Special Interrogatory No. 2 to the jury, using the language, "Were such accumulations retained by plaintiff corporation for the purpose of avoiding the income tax on its stockholder Don Wiener?" Defendant objected to the general charge upon the grounds that it was error as a matter of law to submit such interrogatory to the jury without qualifying and explaining in the instructions that "the purpose" to avoid income tax need not be the dominant or the sole purpose, but it was sufficient if it be one of several purposes. Defendant also requested the Court to give an instruction to this effect. (Defendant's Requested Instruction No. 15.)

* * * *

WHEREFORE, it is prayed (1) that the Court enter a judgment notwithstanding the verdict in favor of the defendant, and (2) in the alternative, that the Court grant defendant a partial new trial on the issue of whether the unreasonable accumulations were for the purpose of avoiding Don Wiener's income tax, or, if the Court determines that it is not possible to grant a partial new trial, a new trial on all issues.

UNITED STATES ATTORNEY

* * * *

HEARING ON MOTION FOR JUDGMENT N.O.V. AND IN THE ALTERNATIVE FOR A PARTIAL NEW TRIAL

(Tr. 580) THE COURT: All right, Mr. White, we will hear your Donruss motion.

That jury is not ready to report?

THE MARSHAL: No, sir.

THE COURT: I was about to say the Court has read your motion and I think is on speaking terms with this matter. But go ahead. We will be glad to hear you.

MR. WHITE: I am sorry. I thought the Court was going to take a report from the jury.

THE COURT: No, I was just inquiring. I got the impression the jury was going to report when the Marshal brought in one of the prisoners.

MR. WHITE: Your Honor, at the outset I would like (Tr. 581) to make a preliminary remark about the instructions the Court gave the jury before talking about the motion. Your Honor will remember the second interrogatory Your Honor submitted asked them were the accumulation of Donruss earnings for the purpose of avoiding the income taxes for the sole shareholder, Mr. Wiener. And we objected to the Court's general charge to the jury after the charge was given, upon the grounds that the Court failed to go forward to explain to the jury that answering this second interrogatory, they should answer "yes," or they should find that the accumulation was for the purpose of avoiding income tax if from the evidence they could discern that one of the reasons for this accumulation was to avoid the income tax. In other words, it did not have to be the sole reason. But if the Donruss Company had ten or twenty reasons for the accumulation and one of the reasons was for the avoidance of income tax—

THE COURT: Well, didn't the Duke—I believe it (Tr. 582) was the Duke case—come into the picture about that?

MR. WHITE: Well, in the Duke case, Your Honor the same interrogatory was given the jury up in Connecticut as you now gave the jury in this case, but that

Court went on to clarify and explain that it is not the sole purpose but it is sufficient if it is one of the purposes.

THE COURT: Well, what other purpose could there have been in this lawsuit?

MR. WHITE: For the accumulation, sir?

THE COURT: Yes, What other purpose? What is in the evidence?

MR. WHITE: Well, I think that the witness testified that he had talked about buying some stock in the Tom Huston Company. And that perhaps is also one of the purposes for the accumulation. And they were afraid of competition. Perhaps that is one of the reasons.

THE COURT: Well, that all merges into the main question, doesn't it?

(Tr. 583) MR. WHITE: Well, I think that the principal question is whether the accumulation was unreasonable. And the jury found the accumulation is unreasonable, taking into consideration all matters that the company planned or stated.

But as to the second question, what might probably have caused them on it some question—and the second question "Was the accumulation for the purpose of avoiding the tax of the Donruss Company?" That is, did plaintiff, Donruss Company—if they could have some purpose in addition to avoidance of income tax, that they are home free insofar as income tax law.

THE COURT: There are many of these things that have slipped the Court's mind, but it just seems to the Court the Duke case pretty well settled this. They were construing the regulations, I believe, in that case.

MR. WHITE: In the Duke case, Your Honor, the exact—

THE COURT: That is—

(Tr. 584) MR. WHITE: The exact question that this Court asked this jury in the Duke case was asked. But the Court in the Duke case went on to explain that if the jury found that this corporation, Duke Laboratories, had several purposes, and one of the many purposes was the avoidance of income taxes, then they had to answer that interrogatory "Yes." In other words, it is not one purpose, but if it is one of many purposes, you see. I assume—

THE COURT: Well, actually, are there any other purposes that there could have been involved here? I just can't—. This was the only question and nothing that I might—

MR. WHITE: Well, Your Honor, I think that the witnesses for the Donruss Company testified on several occasions that they had prospects of buying Tom Huston stock, for instance, and they had talked about it, and that would justify perhaps the accumulation. And if in the proceeding and instruction—and we asked the Court to (Tr. 585) instruct the jury if they answered the Court's interrogatory without these qualifications, if the jury found that the Donruss Company had any other reason other than the avoidance of income taxes for this accumulation, the jury had to answer that question the way they did. But that if the Court—we believe if the Court had instructed the jury that if the Donruss Company had twenty reasons for the accumulation and any of those twenty was for avoidance of tax, then they had to answer that question—.

THE COURT: Well, I don't believe there is anything to that.

Go ahead, then, to something else. I did put up the question to them pretty squarely, I thought. I explained the issues. But go ahead. Let me hear you.

MR. WHITE: No, I am pleased, sir, because this is one of the real crucial points in our argument. But we assume that this statement is an accurate statement of the law, Your Honor.

(Tr. 586) And I was just looking for the Duke Laboratories—I had some language from the instruction in the Duke Laboratories case, to point out to the Court that this Court did not give such an instruction.

This is what the Court of Appeals in the Duke Laboratories case said:

> "Courts should have some reluctance in rewriting statutes. The Congress did not use the article "a" in sections 532 or 533. It did not choose to employ "any" or "dominant" or "primary" purpose. A finding that the accumulations were beyond the reason-

able needs of the business was to "be determinative of the purpose to avoid" unless the taxpayer "by the preponderance of the evidence shall prove to the contrary."

Then the Court comments on the point I am trying to make here:

"The jury was mislead, the Government claims, by (Tr. 587) "the" in the second question."

The Court says this:

"Analysis of the Court's instructions to the jury dispels any such inference. The jury was told that the taxpayer had the burden "to show by a preponderance of the evidence the absence of any intent to avoid the income tax with respect to its shareholders, regardless of whatever other purposes for accumulation the plaintiff may have established."

And then this Court goes on to point out that, as a matter of law, if the interrogatory is given to the jury in the fashion that this Court gave the Donruss jury the interrogatory, that interrogatory has to be explained, has to be qualified in the instructions to the effect that if the jury should find that one of the many purposes was avoidance of tax, then that they must answer the question—

THE COURT: Well, we tried this lawsuit on the one (Tr. 588) purpose theory. I think we did, didn't we?

Mr. Burch, did we do that or not?

MR. BURCH: All or one, if Your Honor please?

THE COURT: However —

MR. BURCH: Yes, sir, all or none, is the way we tried it from the start.

THE COURT: I thought so. I may be in error about it. And I still can't see where there was anything in the proof by which the jury—you did mention the Tom Collins—

MR. WHITE: Huston, Your Honor.

THE COURT: —Tom Huston matter. Then specifically charged the jury with respect to that transaction and told them they could consider that on the question as to whether that—as a part of it.

MR. WHITE: Well, Your Honor, as I understand the way the Court submitted the case to the jury, if the jury would find that one of the purposes for this accumulation —one of the reasons for the accumulation was the pur-
(Tr. 589) pose to buy this Tom Huston stock, then, as a matter of law, they had to answer the interrogatory the way they did. In other words, we believe if the Donruss Company had ten reasons for the accumulation, and one of the ten reasons was to avoid the tax of Don Wiener, then the jury should answer that interrogatory "yes." Plaintiff says if they can show any reason other than the avoidance of income tax, the jury should have answered "no." That is a matter of law.

And, Your Honor, we rely on that statement of law in our motion for judgment NOV. And, upon the assumption that the statement is an accurate statement of the law, we believe we are entitled to judgment NOV for the following reasons: As a matter of law and as a matter of fact in this case, the Donruss Company had actual knowledge that it was avoiding the income tax of Don Wiener by not paying dividends but permitting accumulations to build up as they did. In other words, the corporation we say was placed in the state of mind of actual
(Tr. 590) knowledge that they were avoiding income tax. Now, with respect to the burden of proof in the case, the Donruss Company, as all plaintiffs in tax litigation, or as all plaintiffs in general litigation, had the burden of proving their case by the preponderance of the evidence. But in a 531 case like this, there is a little quirk with regard to the burden of proof. And the Donruss Company in the circumstances of this case is required to prove a negative, the circumstances being that the jury return a finding that it was an unreasonable accumulation.

Now, the fact that it was such unreasonable accumulation, according to the statute, "shall be determinative of the second issue", to-wit, what was the purpose for the accumulation. And the statute referred to states that it shall be determinative unless plaintiff proves by a clear preponderance of the evidence that the unreasonable accumulation was not for the purpose of avoiding taxes.

(Tr. 591) So we believe that this extraordinary burden of proof was demanded as a result of the jury's finding on the first interrogatory, and that actually, the Donruss Company had the burden of proving a negative, which we think was never done here. In other words, we believe that the evidence in the case, from the witnesses, from the documents, when coupled with this actual state of mind, that is, knowing—the knowledge of the Donruss Company that it was avoiding Don Wiener's tax, coupled with the fact that the Donruss Company had to prove a negative—those three things, when put together, and viewing all the evidence in the light most favorable to the plaintiffs and resolving all conflicts in the evidence in favor of plaintiffs, we believe that reasonable men would all contend that this accumulation had as one of its purposes the avoidance of Don Wiener's income tax.

Now, plaintiffs object on three bases—only three bases (Tr. 592) or reasons to the conclusion that we are entitled to a judgment NOV. Their three bases are as follows:

With respect to the first proposition or matter that I took up in the preliminary remarks—I have already talked about this—they say that if they could establish one reason for the accumulation other than the avoidance of tax, then the jury verdict is proper. And we say that if one of the hundreds of reasons for the accumulation was avoidance of tax, then the jury verdict is improper because the plaintiffs have not negated all those things.

The second reason is, plaintiffs say that "We never had the burden of proving a negative in this case." They say that there is nothing more than the normal burden of proof on them. We say, of course, that the statute demanded it.

THE COURT: Well, the Court put the proper burden on them, didn't it?

MR. WHITE: The instructions, yes, Your Honor, you (Tr. 593) correctly stated the point that they had the burden of proving a negative. And the plaintiffs have said that they don't have such a burden. And they cite this Tax Court case. And of course there, as the Court

is aware, the Tax Court rule with regard to the burden of proof in a 531 case is completely different. The rule in the Tax Court places the burden in a 531 case on the Government. And this Tax Court case that is cited by plaintiffs in support of their contention that our proposition was incorrect is discussing—that Casey case is discussing the Tax Court burden of proof.

And finally, they make an observation with regard to our position that the Donruss Company had actual knowledge that they were avoiding Don Wiener's tax. They say—plaintiff says that that is true in every 531 case. Well, it is not true in every one of them. It is only true in your 531 cases where the taxpayer shareholder is also the person who manages the corporation, as here. (Tr. 594) What we are trying to argue for with regard to that proposition is that the Donruss Company had actual knowledge that it was avoiding the shareholder's tax.

So, Your Honor, on those grounds that we have just stated, we believe that we are entitled to judgment NOV and that the Court should enter a judgment in the Government's favor, despite the jury's response to the second interrogatory here.

Now, would the Court desire for me to proceed to discuss the alternative motion at this time, Your Honor please?

THE COURT: Yes, sir, I think so.

MR. WHITE: In the alternative, we move the Court for a partial new trial on the second interrogatory because—that is, whether the accumulation was for the purpose of avoiding the Donruss Corporation's tax, and in the alternative we ask the Court for a whole new trial upon both issues, if the Court is not merely granting a partial new trial.

* * * *

ORDER OVERRULING DEFENDANT'S MOTION FOR JUDGMENT NOTWITHSTANDING THE VERDICT AND IN THE ALTERNATIVE FOR A PARTIAL NEW TRIAL

This cause came on to be heard on the 2nd day of April, 1965 upon the written Motion for Judgment Notwithstanding the Verdict and in the Alternative for a Partial New Trial of defendant in the subject cause, notice of said motion to attorneys for plaintiff herein, and the entire record in this cause, from all of which it appears to the Court that said motion and each and every count thereof is without merit and that said motion should in all things be overruled.

It is, therefore, ORDERED, ADJUDGED AND DECREED that the defendant's Motion for Judgment Notwithstanding the Verdict and in the Alternative for a Partial New Trial in this cause be and the same is hereby overruled.

All of which is ORDERED, ADJUDGED AND DECREED this ____ day of April, 1965.

/s/ MARION S. BOYD
Judge

APPROVED AS TO FORM:

/s/ THOMAS L. ROBINSON
United States Attorney

/s/ TOM MITCHELL, JR.
Attorney for Plaintiff

A TRUE COPY.

ATTEST:

W. LLOYD JOHNSON, Clerk
By V. LAFON, D.C.

• • • •

NOTICE OF APPEAL

Notice is hereby given that the United States of America, defendant, hereby appeals to the United States Court of Appeals for the Sixth Circuit, from the Order Overruling Defendant's Motion For Judgment Notwithstanding The Verdict And In The Alternative For a Partial New Trial, which was entered in this action on April 2, 1965.

This May 28, 1965.

/s/ THOMAS L. ROBINSON
United States Attorney

* * * *

UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

No. 16788

THE DONRUSS COMPANY, PLAINTIFF-APPELLEE

v.

UNITED STATES OF AMERICA, DEFENDANT-APPELLANT

Appeal from the U.S. District Court for the Western District of Tennessee

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Decided September 27, 1967

Before: O'SULLIVAN and CELEBREEZE, Circuit Judges, and BATTISTI, District Judge.*

BATTISTI, District Judge. The Commissioner of Internal Revenue assessed and collected from appellee, The Donruss Company (hereafter Donruss), accumulated earnings taxes for the taxable years 1960 and 1961.

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* Honorable Frank J. Battisti, United States District Judge for the Northern District of Ohio, sitting by designation.

Thereafter, Donruss brought an action for the refund of said taxes in the District Court for the Western District of Tennessee. On the basis of a jury's responses to special interrogatories, the District Court entered judgment for Donruss. The United States appeals.

The interrogatories which were submitted to the jury, and the responses thereto, are as follows:

"1. Did plaintiff corporation permit its earnings or profits for the following years to accumulate beyond the reasonable or reasonably anticipated needs of its business?

	Answer
Year ended January 31, 1960	*Yes*
Year ended January 31, 1961	*Yes*

"2. Were such accumulations retained by plaintiff corporation for the purpose of avoiding the income tax on its shareholder, Don Wiener?

	Answer
Year ended January 31, 1960	*No*
Year ended January 31, 1961	*No* "

In this appeal the Government does not specifically question the propriety of the above-quoted interrogatories. Rather, it urges that the portion of the District Court's general charge explaining the principles underlying the same was misleading and incorrect.

Section 531 of the Internal Revenue Code of 1954 imposes an accumulated earnings tax on every corporation which, as described in Section 532, is "formed or availed of for the purpose of avoiding the income tax with respect to its shareholders * * *, by permitting earnings and profits to accumulate instead of being divided and distributed." Section 533(a) provides that where earnings and profits of a corporation are permitted to accumulate beyond the reasonable needs of the business, this fact "shall be determinative of the purpose to avoid the income tax with respect to shareholders, unless the corporation by the preponderance of the evidence shall prove to the contrary."

The ultimate question in every accumulated earnings tax case is not whether earnings and profits have been accumulated beyond the reasonable needs of the business but whether they have been accumulated for the purpose of avoiding income tax with respect to shareholders. While the reasonableness or unreasonableness of an accumulation is a most significant factor to be considered, particularly with regard to the Section 533(a) presumption, it is not necessarily determinative of the ultimate question, that is to say, whether the corporation was availed of for the proscribed purpose. In *United States* v. *R. C. Tway Coal Sales Co.*, 75 F. 2d 336 (1935) at p. 337, this court said:

> "It is the accumulation of surplus plus its interdicted purpose that brings the statute into operation, and its size in relation to business needs is but a circumstance out of which a presumption of improper purpose arises, though such purpose may be shown by pertinent evidence with or without the presumption as an aid. This view is undoubtedly that of the Court of Appeals of the Second Circuit in *United Business Corp.* v. *Commissioner*, 62 F. 2d 754, 755, and may be accepted as sound. The practical application of the interpretation may, however, in most circumstances be of little importance. The condemned purpose in the forming or utilization of corporations described in the section is the avoidance by stockholders of surtaxes. This purpose may be proved unaided by presumption, but the fact that surplus is not unreasonably large in respect to the needs of the corporation's business is repugnant to the existence of such purpose, and, while not conclusive, must be accepted as substantial evidence in denial of proofs or inferences that it exists."

Thus, if the proscribed purpose is present, the accumulated earnings tax may be imposed even though the accumulation is reasonable. *United States* v. *R. C. Tway Coal Sales Co., supra; Whitney Chain & Mfg. Co.* v. *Commissioner*, 149 F. 2d 936 (C.A. 2 1945); *Pelton Steel Casting Co.* v. *Commissioner*, 251 F. 2d 278 (C.A.

7 1958). On the other hand, if the proscribed purpose is not present, the accumulated earnings tax may not be imposed notwithstanding an unreasonable accumulation. *Duke Laboratories, Inc.* v. *United States*, 337 F. 2d 280 (C.A. 2 1964).

In urging that the District Court's charge was erroneous and misleading, the Government has alluded to certain portions thereof wherein the court discussed the factors which the jury could take into consideration in determining whether earnings and profits were accumulated to meet the "reasonable needs of the business." However, since the jury concluded that the earnings and profits were not accumulated to meet the reasonable needs of the business, any error in this regard would not constitute prejudicial error.

The Government also urges that the charge was erroneous and misleading in that it could have led the jury to conclude that if the accumulations were reasonable there could be no purpose to avoid the tax or, conversely, that if the accumulations were unreasonable the tax should be imposed. For example, the court charged the jury as follows:

> "As stated, Ladies and Gentlemen, the issues in this case arise under the Statutes that Congress has enacted which provide in substance that a corporation must pay a tax called accumulated earnings tax, if it does not distribute to its stockholders all accumulated earnings in excess of what is reasonably needed by the business or in excess of the reasonably anticipated needs of the business." (TR 522)
>
> * * * *
>
> "If, Ladies and Gentlemen of the jury, after a careful consideration of the evidence in the case and the instruction here given you by the Court, you find that the plaintiff taxpayer has shown by the proper quantum of proof, that is, by the greater weight or preponderance of the evidence, that the earnings here in question for the two years under consideration, were accumulated for the purpose of meeting the reasonable business needs or reasonably

anticipated business needs of the plaintiff, The Donruss Company, herein, *rather than* for the purpose of avoiding taxes with respect to its sole shareholder, Mr. Weiner, you will find for the plaintiff, for each year, and report to the Court accordingly." [Emphasis supplied] (TR 535)

When the above-quoted portions of the District Court's charge are read out of context they seem to indicate that the ultimate question the jury was called upon to resolve was whether the accumulations were reasonable or unreasonable. While that would not correctly represent the applicable law, it should be noted that the Government did not object to the charge in that regard, although numerous exceptions were specifically and articulately entered. It is also notable that in various other portions of the charge the District Judge correctly stated the applicable law. For example, the court instructed the jury:

"If you find any of the earnings and profits of the plaintiff for a given year in question were allowed to accumulate beyond the reasonable needs of the business, for that particular year, this shall be determinative of the purpose to avoid the income tax with respect to its sole shareholder, for that year, unless, of course, as the Court has said, that the taxpayer proves the contrary by a preponderance of the evidence." (TR 511)

* * * *

"The issues in this case and the respective contentions of the parties are evidence enough, the Court feels sure. If you find that the plaintiff corporation did accumulate earnings beyond a reasonable present or current needs of its business, or its reasonably anticipated business needs, for the fiscal years ending January 31, 1960 and 1961, and you further find that the purpose of such accumulation was to avoid payment of taxes by the sole shareholder of the plaintiff corporation, Mr. Weiner, then your verdict for each year herein should be for the defendant, The United States of America." (TR 533)

Under Rule 51 of the Federal Rules of Civil Procedure a party who fails to raise a particular objection is deemed to have waived the same. *Transamerica Freight Lines, Inc., et al.* v. *Universal Die Casting Co.*, 192 F. 2d 931 (C.A. 6 1951); *The Sucher Packing Co.* v. *Manufacturers Casualty Insurance Company*, 245 F. 2d 513 (C.A. 6 1957); *McPherson* v. *Hoffman*, 275 F. 2d 466 (C.A. 6 1960); *Solomon* v. *United States*, 276 F. 2d 669 (C.A. 6 1960); *Waxler* v. *Waxler Towing Co.*, 342 F. 2d 746 (C.A. 6 1965). Viewing the District Judge's charge as a whole we are unable to say that the portions quoted above so misled the jury that an abrogation of this principle is warranted. Certainly the fact that able counsel for the Government chose not to object to the same strongly indicates that the charge as a whole did not, as the Government now urges, mislead the jury with regard to a most fundamental question.

Throughout his charge the District Judge instructed the jury that they were required to determine whether Donruss was availed of for "the" purpose of avoiding income tax with respect to its shareholder. At no point during his charge did the District Judge explain to the Jury the significance or meaning of the word "the" as used in the phrase "availed of for the purpose of avoiding income tax." At the conclusion of the charge the Government objected to the same on the ground that the court's failure to so explain the significance or meaning of the word "the" could have led the jury to conclude that avoidance of tax must be the sole purpose behind an accumulation. The Government also objected to the court's failure to give the following Special Request for Instruction:

> "The Court instructs you it is not necessary that avoidance of shareholder's tax be the sole purpose for the unreasonable accumulation of earnings; it is sufficient if it is one of the purposes for the company's accumulation policy."

In the face of the Government's objections the District Judge refused to give any clarification as to the meaning of the phrase "the purpose."

In our view, Sections 531-535 cannot reasonably be construed to require that the purpose to avoid income tax be the sole purpose behind an accumulation before the additional tax may be imposed. Rather, the critical question appears to be whether these sections require that tax avoidance be the dominant, controlling, or impelling purpose behind an accumulation rather than simply "a"[1] purpose. In this regard the authorities differ. In *Trico Products Co.* v. *Commissioner*, 137 F. 2d 424 (C.A. 2 1943) the court stated at p. 426:

> "Nor can we subscribe to the view that the prevention of the imposition of surtaxes must have been shown to have been the dominant factor behind the accumulations."

A similar conclusion was reached in *Barrow Mfg. Co.* v. *Commissioner*, 294 F. 2d 79, 82 (C.A. 5 1961):

> "The Tax Court found, in the language of the statute, that petitioner was availed of 'for the purpose of preventing the imposition of the surtax upon its shareholders.' There was no error in failing to go further and find that that was the primary or dominant purpose of the accumulation. See *Young Motor Co.* v. *Commissioner*, 1960 1 Cir., 281 F. 2d 488, 491. Compare *Kerr-Cochran, Inc.* v. *Commissioner*, 8 Cir. 1958, 253 F. 2d 121, 123. Judge Learned Hand has called attention that this statute 'stands on the footing of the participants' state of mind,' viz., 'the *purpose* of preventing the imposition of the surtax upon its stockholders,' and that it may need the support of presumption, indeed be practically unenforceable without it. * * *' *United Business Corporation* v. *Commissioner*, 2 Cir., 1933, 62 F. 2d 754, 755. The utility of the badly needed presumption arising from the accumulation of earnings or profits beyond the reasonable needs of the business is well nigh destroyed if that presumption in turn is saddled with requirement of proof of 'the primary or dominant purpose' of the accumulation."[1]

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[1] See also, *Mertens*, Section 39.26 and cases cited therein.

The First Circuit reached an opposite conclusion in *Young Motor Co. v. Commissioner*, 281 F. 2d 488, 491 (C.A. 1 1960):

> "The Tax Court may have been led into this error by a misconception of the precise issue. In its opinion it referred to preventing the imposition of the surtax upon stockholders as 'one' of taxpayer's purposes, and stated, 'If this purpose exists it may be accompanied by other legitimate business objectives and still the statute will apply.' The court discussed at some length that taxpayer, being controlled by Young, must be taken to have known that declaring dividends would increase Young's surtaxes—a proposition scarcely requiring argument. If knowledge of such a result is to be the test of purpose, then the only corporations that could safely accumulate income would be those having stockholders with substantial net losses. The statute does not say 'a' purpose, but 'the' purpose. The issue is not what are the necessary, and to that extent contemplated consequences of the accumulation, but what was the primary or diminant purpose which led to the decision. Cf. *Commissioner of Internal Revenue* v. *Duberstein*, 1960, 363 U.S. 278, 80 S. Ct. 1190, 4 L. Ed. 2d 1218. The Tax Court's test was altogether too favorable to the Government."

Authorities holding that the purpose to avoid income tax need not be the dominant, controlling, or impelling motive behind an accumulation seem to originate from an observation made by the Supreme Court in *Helvering* v. *Chicago Stock Yards Co.*, 318 U.S. 693 (1943). In that case, which involved the accumulated earnings tax provisions, the Court sustained a Board of Tax Appeals' finding that the Chicago Stock Yards Company had been availed of for the purpose of avoiding income tax with respect to its shareholder. The Court said in part:

> "A corporate practice adopted for mere convenience or other reasons, and without tax significance when adopted, may have been continued with the

> additional motive of avoiding surtax on the stockholders. The Board's conclusion may justifiably have been reached in the view that, whatever the motive when the practice of accumulation was adopted, the purpose of avoiding surtax induced, *or aided in inducing*, the continuance of the practice." (318 U.S., 698, 699.) [Emphasis supplied.]

The Court's language clearly implies that the purpose to avoid income tax need not be the sole purpose behind an accumulation in order for the additional tax to be imposed. However, it would greatly strain the Court's remarks to conclude that on so employing the parenthetical phrase "or aided in inducing," it was considering the important question here posed, that is to say, whether the purpose to avoid income tax need be the dominant, controlling, or impelling purpose.

There are a number of instances where motivation is the relevant consideration in determining the tax consequences of a individual's conduct. For example, 26 U.S. C.A., Section 2035(a) provides for the inclusion of property in the gross estate of a decedent "to the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, in contemplation of his death." Section 2035(a) does not by its terms require the inclusion within the gross estate of property transferred "solely" or "predominately" in contemplation of death. Nonetheless, it has been held consistently that the death motive must be the dominant, controlling, or impelling motive behind the transfer in order for it to be deemed a transfer in contemplation of death. *United States* v. *Wells*, 283 U.S. 102 (1931); *City Bank Farmer's Trust Co.* v. *McGowan*, 323 U.S. 594 (1944); *Allen* v. *Trust Company of Georgia, et al.*, 326 U.S. 630 (1946). Further, in determining whether the transfer of property by an individual is a gift within the meaning of 26 U.S. C.A., Section 102(a) "the proper criterion * * * is one that inquires what the basic reason for his conduct was in fact—the dominant reason that explains his action in

making the transfer." *Commissioner* v. *Duberstein*, 363 U.S. 278, 286 (1960).

In our view there is no sound reason why the "dominant, controlling, or impelling" motive test employed in connection with the gift in contemplation of death provision should not be applied to the accumulated earnings tax provision. Both provisions have as their underlying purpose the prevention of tax avoidance which is made possible by the structure of the income tax laws. Neither provision explicitly sets out the extent to which the proscribed purpose must play a part in the transaction or conduct in order for the tax consequences to attach. To hold that the dominant, controlling, or impelling motive criterion is inapplicable in the case of the accumulated earnings tax provision would require that we make a distinction where no material difference exists. Accordingly, we conclude that tax avoidance must be the dominant, controlling, or impelling motive behind an accumulation in order to impose the accumulated earnings tax.

Throughout his charge the District Judge spoke in terms of the taxpayer being "availed of for the purpose of avoiding the income tax with respect to its shareholder." As witnessed by our previous discussion, this language is subject to a number of interpretations. At the conclusion of the charge, counsel for the Government called the court's attention to this fact and, in substance, asked that the jury be given the benefit of an interpretation of the language. The District Judge failed to give such an interpretation.

Considering the District Judge's charge as a whole, we are of the opinion that the jury might well have been led to believe that tax avoidance must be the sole purpose behind an accumulation in order to impose the accumulated earnings tax. While it was entirely proper for the District Judge to use the exact language of the statute in the course of his charge, it was prejudicial error not to clarify the crucial statutory language which was clearly subject to more than one interpretation, particularly when the problem had been called to his attention. Ac-

cordingly, the judgment of the District Court is reversed and the case remanded for a new trial.[2]

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[2] Having reached this conclusion, it is unnecessary to consider or pass upon the arguments made by the Government in connection with the District Court's denial of a request for a continuance and also its efforts to impeach the jury's verdict.

UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

No. 16,788

THE DONRUSS COMPANY, PLAINTIFF-APPELLEE

v.

UNITED STATES OF AMERICA, DEFENDANT-APPELLANT

Before: O'SULLIVAN and CELEBREZZE, Circuit Judges and BATTISTI, District Judge.

JUDGMENT

Appeal from the United States District Court for the Western District of Tennessee.

This Cause came on to be heard on the record from the United States District Court for the Western District of Tennessee and was argued by counsel.

On consideration whereof, It is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be and the same is hereby reversed and the case remanded for a new trial.

No costs awarded. Rule 23(4).

Entered by order of the Court.

CARL W. REUSS, *Clerk.*

A true copy.

Attest:

CARL W. REUSS, *Clerk.*

SUPREME COURT OF THE UNITED STATES

No. 963, October Term, 1967

UNITED STATES, PETITIONER

v.

THE DONRUSS COMPANY

ORDER ALLOWING CERTIORARI—Filed April 22, 1968

The petition herein for a writ of certiorari to the United States Court of Appeals for the Sixth Circuit is granted, and the case is placed on the summary calendar.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

☆ U. S. GOVERNMENT PRINTING OFFICE: 1968 298483 765